1998 ANNUAL REPORT

H&R REAL ESTATE INVESTMENT TRUST

BUILDING ON EXPERIENCE

H&R REAL ESTATE INVESTMENT TRUST

Incorporated on November 4, 1996, H&R Real Estate Investment Trust ("H&R REIT") owns and manages a portfolio of income-producing properties and provides mezzanine financing for development projects. As of December 31, 1998, H&R REIT held interests in 20 office properties, 32 single-tenant industrial properties, three retail properties, and eight development projects.

As a closed-end REIT, a substantial proportion of H&R REIT's cash is distributed to Unitholders each month, and much of it is tax deferred.

The REIT's internal management conducts the day-to-day operations and growth of H&R REIT at the direction of the Board of Trustees. Investments are governed by specific guidelines and are subject to the approval of the Trustees.

Units of the Trust trade on The Toronto Stock Exchange (Symbol: HR.UN).

250 University Avenue, Toronto

Contents

Highlights

- Cash flow from operations increased 125% to $38 million or $1.21 per unit. Distributable income increased 141% to $35.9 million or $1.15 per unit.

- Distributions to Unitholders, now paid monthly, increased from $0.68 per unit in 1997 to $1.03 in 1998, a 37% increase on a fully paid basis. The current distribution is $0.092 per month or $1.104 on an annualized basis.

- The REIT acquired six office properties, six single-tenant industrial properties and two retail properties at a total cost of $150.0 million, increasing gross leasable area by 42% to 6.7 million square feet.

- H&R REIT provided $65.0 million in initial financing to begin construction of the one million square foot TransCanada PipeLines Tower in Calgary. The REIT has an option to purchase this landmark building at cost, which should generate leveraged returns of approximately 17% when acquired.

- We invested an additional $85 million in six other development projects where H&R REIT is utilizing its development expertise to achieve superior returns for Unitholders without deviating from its established risk profile.

Objectives

H&R Real Estate Investment Trust has two main objectives:

First, to provide unitholders with reliable and growing tax-deferred cash distributions from its portfolio of income producing properties.

Second, to increase the value of units through active management of the REIT's assets and the acquisition of additional properties.

Management is committed to maximizing cash distributions and capital appreciation while maintaining prudent risk management and conservative use of financial leverage.

Report to Unitholders

1998 was a very successful year for H&R REIT. We achieved our goals of delivering increased value and cash distributions to our Unitholders by executing strategic, accretive acquisitions designed to increase our portfolio of quality assets and by enhancing the value of our properties.

Our 1998 activities have left us well positioned to further grow our distributable income and unit value. H&R REIT's fundamental philosophy and investment criteria remains unchanged: to maintain a tenant base of long-term, creditworthy occupants that ensures the sustainability of our reliable, secure and growing cash flow.

FINANCIAL RESULTS

H&R REIT achieved record financial results in net income and distributions in absolute and per unit terms. Revenue from income producing properties increased 51% to $93.4 million, reflecting our successful acquisition program and contracted rental increases. This revenue growth translated into an improvement in cash flow and distributable income. Cash flow from operations increased 125% to $38 million or $1.21 per unit while distributable income increased 141% to $35.9 million or $1.15 per unit. Most importantly for Unitholders, total cash distributions grew 37% on a fully-paid basis (51% for those who purchased the initial instalment receipts) to $1.03 per unit, while still maintaining H&R REIT's conservative policy of paying out 90% of distributable income.

TRANSCANADA PIPELINES TOWER

In 1998, H&R REIT announced the largest and most exciting transaction in its history: the financing and subsequent ownership of the new head office for TransCanada PipeLines (TCPL) in downtown Calgary. This prestigious one million square foot, Class A, trophy development is the largest pre-leased office project in Canada today. Importantly, this ambitious project is being effected through a structure designed to shelter the REIT from financial risk.

H&R REIT provided $65 million in financing which is secured by the assignment of the lease and a mortgage on the property that will earn the REIT an initial unleveraged return on investment of 10%. Upon completion and occupancy of the project, in the summer of 2001, H&R REIT can exercise its option to purchase the development at a price equal to the total development cost of the project. The building has been pre-leased to TCPL for 20 years, with built-in contractual rent increases every five years. We anticipate that, when fully occupied and appropriately financed, this project will provide a return of approximately 17% to the REIT.

This transaction is a watershed for H&R REIT. Without deviating from our philosophy or risk profile, we have successfully initiated this trophy development at a yield that will be highly accretive to the REIT.. As a result of this innovative development, we expect the REIT's hightened profile to lead to many future opportunities.

TransCanada PipeLines Tower, Calgary

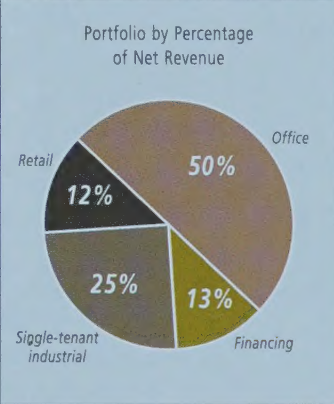
310-320-330 Front St. West, Toronto

ACCRETIVE ACQUISITIONS

After our first full year of operations ended December 31, 1997, H&R REIT's 4.8 million square foot portfolio consisted of 14 office properties, 26 single-tenant industrial properties and one retail property. At the beginning of 1998, our portfolio included such prominent properties as;

- the REIT's first retail property at 110 Bloor Street West, in the heart of Toronto's high-fashion district – a three-storey, 85,176 square foot building that features the Canadian flagship store for Chapters bookstores, as well as the newly opened Nike store, Escada and Louis Vuitton
- 310-320-330 Front Street West, a 567,861 square foot office building in downtown Toronto, situated directly across the street from the SkyDome
- the head office for Nestlé Canada, a 359,227 square foot building at Yonge and Sheppard in Toronto.

In 1998, we grew our portfolio by 42% through the addition of six office properties, six single-tenant industrial properties and two retail properties increasing our total leasable area to 6.7 million square feet. Each acquisition was consistent with our objective of investing in properties that are leased to long-term, creditworthy tenants and are immediately accretive to our distributable income. These acquisitions increased the book value of our revenue-producing assets by 33% to $585.3 million and will continue to provide sustained and growing revenue and distributable income to the REIT.



As an example of the implementation of our conservative acquisition criteria, in 1998, the REIT purchased 250 University Avenue, a prestigious 132,000 square foot office property in downtown Toronto, for $16.5 million, or $125 per square foot, leased to King's Health Care for an initial term of 20 years and with contractual rental increases every five years; and, two single-tenant industrial properties, totaling 392,603 square feet, for $20.9 million, located in Quebec, and leased to ASEA Brown Boveri Inc.(ABB) for a term of 15 years with contractual rental increases every five years. These transactions have provided the REIT with a return on equity of 18% and 26% respectively, financed with fixed rate long-term mortgages that mirror the properties' lease expiries.

In addition to our acquisition program, we provided mezzanine financing for seven development projects, including the TransCanada PipeLines Tower. These projects enable the REIT to achieve enhanced yields by investing in projects earlier in the development process and utilize H&R's extensive development expertise to see the project through to completion. As a result, the REIT can achieve up to an additional 150-200 basis points in unleveraged yield. Moreover, the REIT will not finance a development project with the intention of acquiring it unless, and until, the project has appropriate pre-leasing to minimize risk. Specifically, the REIT will not provide construction financing unless 70% of the project has been pre-leased.

Report to Unitholders

To fund our acquisition program, the REIT raised a total of $147 million in 1998 through two unit offerings, $100 million completed on May 21 and $47 million on December 10. The ability to raise money through two unit offerings in 1998 distinguished H&R REIT from its peer group, for whom equity markets were not equally accessible. As a result, we were able to fund growth and take advantage of opportunities that others were precluded from pursuing, due to a lack of financing. Importantly, the strong returns generated by our acquisitions led to increased cash flow and distributions on a per unit basis, with no dilutive effect. We increased our distribution from $0.68 per unit to $1.03 per unit and, in April, began to distribute on a monthly basis. Moreover, in December we increased the monthly payout to $0.092 per unit, or $1.104 on an annualized basis, further reflecting the successful use of proceeds of these offerings.

25 Sheppard Avenue West, Toronto

MARKET OVERVIEW

With low interest and vacancy rates, real estate fundamentals remained strong in 1998 leaving the industry well positioned to continue its strong growth in 1999. Unlike the early 1990's, when the industry was caught with oversupply and an under-performing economy, the discipline of the debt and equity markets resulted in a better balance of supply and demand.

In 1999, we believe that many real estate companies and REITs, for whom the equity markets are not accessible, will begin closely scrutinizing their properties to identify assets for potential disposition. H&R REIT will selectively analyze investment opportunities to assess their merit against our investment criteria. We are well positioned to take advantage of upcoming investment opportunities with our strong balance sheet, debt capacity and proven ability to raise equity.

OUR STRATEGY

H&R REIT's 1998 results illustrate that our acquisition and portfolio management strategies lead to success. We will maintain the investment philosophy that has characterized H&R REIT since its inception.

We are clearly focused on acquisitions that offer both immediately accretive returns and on-going potential for growth in distributable income, without assuming undue risk. We execute this strategy by investing primarily in properties at prices less than, or equal to, replacement cost occupied by high-quality, creditworthy tenants signed to long-term leases. This is real estate that will appreciate over time and produce consistent growth for our Unitholders. In 1998, our portfolio maintained an average occupancy of 99% and only 27% of our leases will mature over the next five years. While our portfolio is still heavily weighted towards the Greater Toronto Area, we are geographically diversifying the portfolio by taking advantage of a number of opportunities in markets across Canada.

The REIT will continue to benefit from management's development expertise to incrementally enhance returns by acquiring properties in the development phase. To maintain a risk profile consistent with the objectives of the REIT, and in accordance with the Trust's indenture guidelines, we will not fund the development of a project until significant levels of pre-leasing have been achieved. The development of the TransCanada PipeLines Tower illustrates the competitive advantage of H&R REIT in executing this strategy.

We are securing our long-term growth by managing our risk profile and using financial leverage conservatively. We have reduced the uncertainty associated with fluctuations in real estate and interest rates by prudently matching lease terms to debt maturity. The weighted average term to maturity of our mortgages of 10.6 years closely matches the remaining average lease term of our tenancies of 9.4 years. Furthermore, in accordance with our trust guidelines, we limit debt secured by our property portfolio to a maximum of 60 per cent of the REIT's gross book assets. At December 31, 1998, this percentage was a conservative 45%.

We are demonstrating our commitment to Unitholders by maintaining general, administrative and property management expenses at approximately 7% of gross revenue; making H&R REIT one of the most cost-effective in the industry.

LOOKING FORWARD

I am optimistic that 1999 will be a year of continued success for H&R REIT.

The development of the TransCanada PipeLines Tower elevates us to the next level by proving we have the expertise to develop landmark properties and achieve well-above-market yields while assuming no additional risk.

H&R REIT has continued to achieve its objective of maximizing Unitholder value by adhering to its operating philosophy of acquiring commercial properties leased to long-term, creditworthy tenants that are accretive to our distributable income. We will continue to follow this proven strategy for success.

Finally, I would like to thank the Board of Trustees and our employees for their dedication and hard work in building H&R REIT. I would also like to thank our tenants and stakeholders whose confidence and support have contributed to our success.

Thomas J. Hofstedter
President and Chief Executive Officer

Portfolio

OFFICE PROPERTIES

As at December 31, 1998

Properties	Ownership Interest	Year Built	Net Rentable Area (square feet)	Occupancy	Major Tenants	Occupancy by Major Tenants
310-320-330 Front St. W. Toronto, ON	70%	1989-1990.	567,861	97%	Two Canadian banks, Air Canada, NCR, Lumberman's Mutual	81%
401-405 The West Mall Etobicoke ON	70%	1983-1985.	410,784	100%	Livingston International, Parmalat Food, an insurance company, Canada Starch, Consumers Packaging, Gilbey Canada	64%
25 Sheppard Ave. W. North York, ON	70%	1994	359,227	100%	Nestlé Canada, Telemedia, Hewitt & Associates, Association of Professional Engineers of Ontario	85%
26 Wellington St. E. Toronto, ON	70%	1981	172,353	99%	An insurance company, United Way, Sceptre Investments	62%
55 Yonge St. Toronto, ON	70%	1956	154,890	100%	A Canadian bank, TransCanada PipeLines, Telerate Canada, Western Gas, BPI Financial	87%
145 Wellington St. W Toronto, ON	70%	1987	153,314	100%	An insurance company, Aon Consulting Inc.	74%
110 Sheppard Ave. E North York, ON	50%	1993	145,116	100%	Equifax Canada Inc., Wyeth-Ayerst Canada Inc.	97%
2810 Matheson Blvd. E. Mississauga, ON	35%	1990	140,210	98%	Credit Union Central of Ontario	70%
250 University Ave. Toronto, ON	100%	1958	132,000	100%	King's Health Centre Corp.	100%
2780-2800 Skymark Ave. Mississauga, ON	60%	1988-1990	109,018	99%	Starber-Fritz Inc., Nordic Tours, a Canadian Bank, McDonald's	33%
2611-3rd Ave. Calgary, AB	50%	1998	95,465	100%	Telus Advertising Services Inc.	100%
631 South Olive St.* Los Angeles, CA	100%	1986	91,611	93%	The NBBJ Group, M.K. Diamonds	17%
1235 Bay St. Toronto, ON	100%	1973	91,108	89%	Dental Anesthesia Assoc., Interac Business Centres, Walt Disney (Canada) Ltd.	30%
69 Yonge St. Toronto, ON	70%	1914	85,151	86%	Livingston Group, Shoppers Drug Mart	31%
1 Kenview Blvd. Brampton, ON	100%	1989	79,005	100%	Atlantis Aerospace Corp.	100%
291-295 The West Mall Etobicoke, ON	70%	1978	77,345	93%	Parmalat Food, Investors Group Financial Services	35%
3625 Dufferin St. North York, ON	70%	1965	71,288	79%	H&R Property Management Ltd.	32%
88 McNabb St. Markham, ON	70%	1987	69,865	100%	Wyeth-Ayerst Canada Inc.	100%
2767-2nd Ave. Calgary, AB	100%	1998	69,630	100%	DeVry Inc.	100%
131 McNabb St. Markham, ON	100%	1989	54,100	100%	Drug Trading Company Ltd.	100%
Total			3,129,341	98%		

** Held through a wholly-owned U.S. subsidiary.*

SINGLE-TENANT INDUSTRIAL PROPERTIES

As at December 31, 1998

Properties	Ownership Interest	Year Built/ Renovated	Net Rentable Area (square feet)	Occupancy	Major Tenants	Occupancy by Major Tenants
55 West Drive Brampton, ON	100%	1969/ 1981	505,565	100%	Winners Apparel Ltd.	100%
4441-76th St. Calgary, AB	100%	1980	323,796	100%	TCT Logistics Inc., Livingston Distribution Centres Inc.	100%
137 Horner Ave. Etobicoke, ON	100%	1962	320,000	100%	TCT Logistics Inc.	100%
2121 Cornwall Rd. Oakville, ON	100%	1997-1998	314,165	100%	Livingston Logistics Services Inc.	100%
1600 Lionell Boulet Varennes, PQ	100%	1971	311,103	100%	ASEA Brown Boveri Inc.	100%
1450 Mountain Ave. Winnipeg, MB	100%	1973	266,102	100%	Palliser Furniture	100%
7830 Tranmere Dr. Mississauga, ON	100%	1985/ 1987	265,469	100%	Paperboard Industries Corporation	100%
75 Frontenac Dr. Markham, ON	100%	1986	247,556	100%	Hyundai Auto Canada	100%
3655 Weston Rd. Downsview, ON	100%	1970	184,266	100%	O.S.F. Inc.	100%
2390 Argentia Rd. Mississauga, ON	100%	1984	179,085	100%	Northern Telecom Ltd.	100%
351 Passmore Ave. Scarborough, ON	100%	1986	161,137	100%	Slater Steel Inc.	100%
11 Kenview Blvd. Brampton, ON	100%	1989	139,548	100%	Para Paints Canada Inc. GBC Canada Inc.	100%
10920-178th St. Edmonton, AB	100%	1987	131,475	100%	TCT Logistics Inc.	100%
2841 Langstaff Rd. Vaughan, ON	100%	1996	123,906	100%	Minuk Contruction and Engineering, Planet Paper Box Inc.	100%
1350-1380 Matheson Blvd. E. and 5391 Ambler Dr., Mississauga, ON	100%	1987	110,059	100%	Minuk Construction and Engineering	100%
10300 Henri Bourassa St. Laurent, PQ	100%	1976/ 1989	81,500	100%	ASEA Brown Boveri Inc.	100%
2 East Beaver Creek Rd. Richmond Hill, ON	70%	1988	78,982	100%	Country Style Donuts, Phonettix Intelecom, Pureco Labs, Motorola	100%
1060 Tristar Dr. Mississauga, ON	100%	1984	65,284	100%	Clarke Lithographing Ltd.	100%
880 Milner Ave. Scarborough, ON	70%	1990	60,028	100%	House of Electrical, G.H. Import	100%
2860 Plymouth Dr. Oakville, ON	100%	1989	59,613	100%	Garlock of Canada	100%
1 Moyal Court Vaughan, ON	70%	1991	52,792	100%	Wajax Industries Limited	100%

Portfolio

SINGLE-TENANT INDUSTRIAL PROPERTIES - contd.

As at December 31, 1998

Properties	Ownership Interest	Year Built/ Renovated	Net Rentable Area (Square Feet)	Occupancy	Major Tenants	Occupancy by Major Tenants
5 Bodrington Crt. Markham, ON	70%	1994	50,000	100%	Belmont Press	100%
360 Spinnaker Way Vaughan, ON	70%	1995	41,944	100%	The Packaging Group	100%
2815 Matheson Blvd. E Mississauga, ON	70%	1987	40,000	100%	ADT Secuntry Services	100%
388 Spinnaker Way Vaughan, ON	70%	1995	37,383	100%	Bennett Tools	100%
380 Spinnaker Way Vaughan, ON	70%	1995	33,017	100%	Topax Export Packaging	100%
4248-14th Ave. Markham, ON	70%	1994	32,708	100%	Linsey Foods Limited	100%
300 Biscayne Cres. Brampton, ON	70%	1996	31,606	100%	Dicom Express Inc.	100%
45 Bodrington Crt. Markham, ON	70%	1992	28,089	100%	Corporate Foods Limited	100%
75 Addiscott Rd. Markham, ON	70%	1996	27,627	100%	Riviera Catering	100%
2400 Matheson Blvd. E Mississauga, ON	70%	1993	25,000	100%	Kambria Controls	100%
5230 Orbitor Dr. Mississauga, ON	70%	1994	22,000	100%	W.K. Buckley Limited	100%
Total			4,350,805	100%		

RETAIL PROPERTIES

720 Maloney Blvd. W. Gatineau, PQ	50%	1995-1998	279,242	100%	Wal-Mart, Canadian Tire, Metro Richlieu	93%
220 Chain Lake Dr. Halifax, NS	50%	1996-1998	135,453	100%	Wal-Mart	98%
110 Bloor St. W. Toronto, ON	100%	1997-1998	85,176	100%	Chapters, Nike, Escada, Louis Vuitton	97%
Total			499,871	100%		

Portfolio

2780-2800 Skymark Avenue, Mississauga

145 Wellington Street West, Toronto

110 Bloor Street West, Toronto

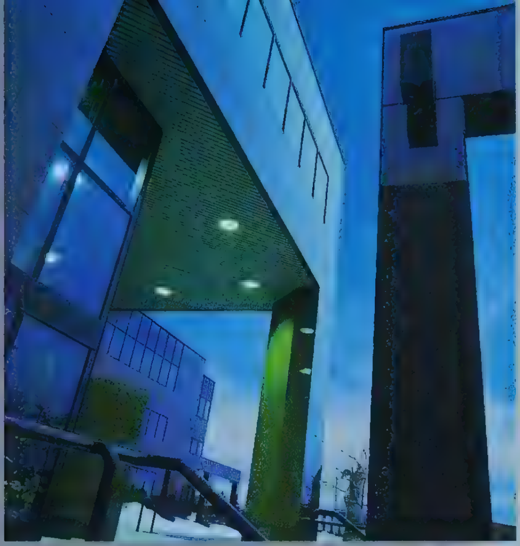
250 University Avenue, Toronto

Portfolio

131 McNabb Street, Markham

110 Sheppard Avenue East, North York

310-320-330 Front Street West, Toronto



1 Kenview Boulevard, Brampton

25 Sheppard Avenue West, Toronto

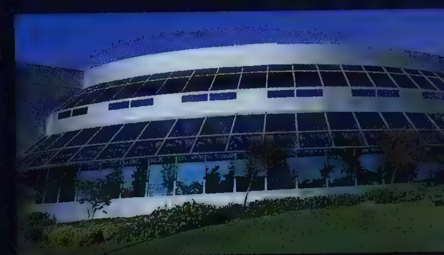
88 McNabb Street, Markham

2400 Matheson Boulevard East, Mississauga

2860 Plymouth Drive, Oakville

26 Wellington Street East, Toronto

7830 Tranmere Drive, Mississauga



11 Kenview Boulevard, Brampton

2810 Matheson Boulevard East, Mississauga

351 Passmore Avenue, Scarborough

631 South Olive Street, Los Angeles

1600 Lionell Boulet, Varennes

Portfolio

OVERVIEW OF PORTFOLIO

The following table summarizes the Portfolio of the REIT as at December 31, 1998.
[Net ownership position]

Portfolio	Office	Single-Tenant Industrial	Retail	Total
Number of Properties	20	32	3	55
Total Leasable Area (square feet)	2,248,149	4,181,486	292,386	6,722,021
Occupancy*	98%	100%	100%	99%
Average Rent in Place	$ 15.41	$ 3.98	$ 20.14	$ 8.51
Average Interest Rate on Outstanding Mortgages*	9.5%	7.2%	7.0%	8.9%

* Weighted Average

LEASE MATURITIES

Portfolio	Office*	Single-Tenant Industrial*	Retail*	Total*
1999	2.2%	0.8%	-	3.0%
2000	2.4%	0.6%	-	3.0%
2001	2.0%	-	-	2.0%
2002	3.5%	7.2%	0.1%	10.8%
2003	3.4%	4.9%	-	8.3%

*Percent of total leasable area of portfolio.

DEBT MATURITIES

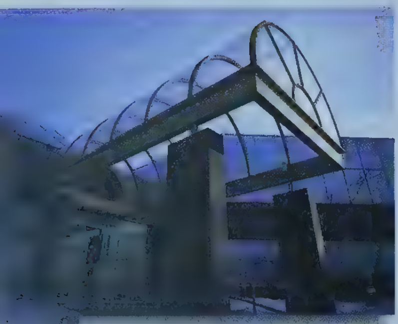
The following table summarizes the debt maturities for the properties of the REIT on a combined basis, exclusive of normal monthly self-amortizing principal repayments.

Portfolio	Office	Single-Tenant Industrial	Retail	Total	Percentage of Mortgages Outstanding
1999	$ 3,250,000	$ 8,773,055	-	$ 12,023,055	4.2%
2000	13,829,375	9,113,783	-	22,943,158	8.1%
2001	21,415,614	2,076,808	-	23,492,422	8.2%
2002	-	7,651,265	-	7,651,265	2.7%
2003	-	1,810,922	-	1,810,922	0.6%

Management's Discussion and Analysis

OVERVIEW

H&R Real Estate Investment Trust (the "REIT") is an unincorporated closed-end trust created by a Declaration of Trust and governed by the laws of the Province of Ontario.



131 McNabb Street, Markham

The REIT commenced operations on December 23, 1996 with the initial acquisition of a 70% undivided interest in a portfolio of 27 properties principally located in the Greater Toronto Area. As at December 31, 1998, the REIT owned and operated a portfolio of 55 properties (20 office, 32 single-tenant industrial and three retail) comprising an aggregate leaseable area of 6.7 million square feet (as calculated at the REIT's level of ownership.) Three single-tenant industrial properties and two office properties are located in Western Canada, two single-tenant industrial and two retail properties are located in Eastern Canada and one office property is situated in Los Angeles, California. The balance of the properties are located in the Greater Toronto Area.

The REIT's primary objectives are to provide Unitholders with stable and growing cash distributions and to maximize unit value through ongoing active management of the REIT's assets, future acquisitions of additional properties and the development of new properties on a selective basis.

NET EARNINGS AND FINANCIAL POSITION

The financial information as at December 31, 1998 and the results of operations for the year then ended are presented in accordance with accounting principles applicable to real estate investment trusts. The following discussion should be read in conjunction with the REIT's financial statements for the year ended December 31, 1998 and 1997.

RESULT OF OPERATIONS

Net earnings for the year ended December 31, 1998 of $34.1 million, or $1.09 per Unit, increased by 107% on a dollar basis and 30% on a per Unit basis over the $16.5 million, $0.84 per unit, for December 31, 1997. Depreciation of $3.8 million (1997 $2.4 million) and amortization of $0.5 million (1997 $0.1 million) are included in the determination of net income. The REIT does not take depreciation expense into account when calculating distributions paid to Unitholders.

Income from Rental Operations Before Depreciation & Amortization (000's)	1998	1997
Rentals from income properties	$ 93,432	$ 62,012
Mortgage interest income and other	8,129	580
	101,561	62,592
Property operating costs	38,141	24,584
Operating income before interest	63,420	38,008
Mortgage and other interest	21,939	19,367
Income from operations before depreciation and amortization	$ 41,481	$ 18,641

RENTALS FROM INCOME PROPERTIES

Rental income from income properties increased 51% from $62.0 million in 1997 to $93.4 million in 1998. The increase is primarily a result of the REIT's ongoing acquisition program that totaled $150.0 million in 1998. Property operating costs and mortgage and other interest have also increased proportionately from $24.6 million and $19.4 million in 1997, to $38.1 million and $21.9 million respectively in 1998.

The overall occupancy rate in the REIT's portfolio was 99% at December 31, 1998 compared to 98% the prior year. The exposure to lease rollovers, as a result of lease expiries, over the next 5 years (as a percentage of the REIT owned portion of the properties) is as follows:

1999	3.0%
2000	3.0%
2001	2.0%
2002	10.8%
2003	8.3%


11 Kenview Boulevard, Brampton

MORTGAGE INTEREST INCOME

The REIT earned $7.7 million in mortgage interest income in 1998 reflecting the incorporation of development as an integral part of the REIT's operations during 1998. Included in this amount is $2.0 million earned from the mezzanine financing for the TransCanada PipeLines Tower project (TCPL project), the largest single transaction in the REIT's history. The weighted average interest rate earned on these investments in 1998 was approximately 9.9%. For details on mortgage receivable activity in the year, see Mortgages Receivable below.

SALE OF INCOME PROPERTIES

The REIT will dispose of non-strategic assets that no longer fit its investment strategy and then redeploy those proceeds in better investment opportunities. In December 1998, the REIT sold a multi-tenant industrial property located in Mississauga, Ontario and realized a gain of $0.4 million.

GENERAL AND ADMINISTRATIVE TRUST EXPENSES

General and administrative expenses increased during the year from $1.7 million to $3.1 million. While these expenses have increased during the year, they remained relatively stable as a percentage of gross assets 0.4% (1997 0.4%) and of total revenue 3.1% (1997 2.7%).

OTHER INCOME

The instalment receipts issued in 1996 and 1997 were fully paid on December 23, 1997 and the related interest income of $2.0 million therefore did not reoccur in 1998.

DISTRIBUTION TO UNITHOLDERS

The policy of the REIT is to distribute 90% of its income to Unitholders on a monthly basis. Depreciation and other non-cash items are added to, or deducted from, net earnings to determine the amount of income for distribution to Unitholders in accordance with the distribution policy of the REIT.

Calculation of distributable income for the years ended December 31,

(000's)	1998	1997
Net earnings	$ 34,059	$ 16,460
Add (deduct)		
Depreciation	3,817	2,370
Accrued rent	(2,138)	(2,109)
Imputed mortgage interest	202	220
Instalment receipt interest income	-	(2,041)
Distributable income	$ 35,940	$ 14,900

Management's Discussion and Analysis

Accrued rent represents the adjustment made to normalize rents for certain tenants whose rental rate increases substantially over the term of their respective leases. This adjustment is required by GAAP and represents a non-cash item to be deducted in determining distributable income.

Total distributions per unit for 1998, calculated at 90% of distributable income, were $1.03 per unit, compared to $0.68 per unit in 1997; a 51% increase. The tax deferred portion of the distribution was 62% compared to 100% in 1997. This deferral will vary in any given year due to factors such as the size and timing of unit offerings and acquisitions of properties.

CHANGES IN FINANCIAL POSITION

ASSETS

Income Properties

The REIT acquired 14 properties during the year and disposed of one. The acquisitions followed the REIT's investment strategy of acquiring quality assets occupied by long-term creditworthy tenants. These acquisitions impacted all three of the REIT's property categories: office, single-tenant and retail. Funds for these purchases were provided by two public offerings in May and December 1998. As a result, income properties increased by 32.8% to $585.3 million at December 31, 1998 from $440.5 million at December 31, 1997.


2390 Argentia Road, Mississ

In April 1998, the REIT purchased a 100% interest in two single-tenant industrial properties and a 50% interest in two retail properties anchored by Wal-Mart. The single-tenant industrial properties comprising 124,897 square feet, are located in Oakville and Mississauga, Ontario and are leased until 2005 and 2009 to Garlock of Canada Limited and Clarke Lithographing Ltd. respectively. The Wal-Mart properties added 207,348 square feet to the REIT's portfolio and are situated in Gatineau, Quebec and Halifax, Nova Scotia with 20 year leases in place.

During May 1998, the REIT acquired 100% interest in a 505,565 single-tenant industrial building located in Brampton, Ontario leased to Winners Apparel until 2008. In the same month, the REIT also purchased a 91,108 square foot office building located at Bay and Bloor Streets in Toronto, Ontario leased to a mix of smaller tenants with lease terms between 3 and 5 years.

In June 1998, the REIT purchased a 132,000 square foot office property located at 250 University Avenue, Toronto, Ontario leased to the King's Health Care Corporation for a 20 year period.

In August 1998, the REIT purchased a 247,556 square foot single-tenant industrial building in Markham, Ontario. This property is leased to the Hyundai Motor Company until August 2009.

In September 1998, the first of two office properties in Calgary, Alberta was purchased from a single vendor. DeVry Inc. occupies this 69,630 square foot building under a 15 year lease maturing in 2013.

Two suburban office properties located in Markham and Brampton, Ontario totalling 133,105 square feet were purchased from two separate vendors in November 1998. The Markham building has a rentable area of 54,100 square feet and is leased to Drug Trading Company Limited until January 2011. The 79,005 square foot Brampton property was purchased for cash and the assumption of debt and is leased to Atlantis Aerospace Corporation until 2013.

Finally, during December 1998, the REIT completed the purchase of a 50% interest in a second office property in Calgary, Alberta and a 100% interest in two single-tenant industrial properties in Quebec. The 95,465 square foot Calgary property is leased to Telus Advertising Services for a 15 year term. The two single-tenant industrial properties have a combined leaseable area of 392,603 square feet and are leased for 15 years to ASEA Brown Boveri Inc.

10300 Henri Bourassa, St. Laurent

Mortgages Receivables

During 1998, the REIT continued the program it started in December 1997 of providing mezzanine financing for development projects that are consistent with the REIT's objectives and philosophy. These projects are secured through mortgage financing provided by the REIT, which receives or anticipates receiving an option to acquire an equity interest in the project. Construction financing will only be provided once 70% of the project has been pre-leased. Participation in development projects will enable the REIT to acquire high-quality properties at higher yields than would otherwise be available.

Mortgages receivables have increased from a single development of $8.3 million on Millcreek Drive in Mississauga in December 31, 1997 to eight developments comprising $153.1 million at December 31, 1998. The largest of these transactions comprises the $65.0 million financing for the development of the new head office of TransCanada PipeLines in Calgary, Alberta. The financing was advanced in September 1998 in return for an option to purchase the fully leased project at cost, upon expected completion in the summer/fall of 2001.

Other transactions included the following:

In March 1998, $16.0 million was provided for the development of a 66.4 acre retail centre in Calgary, Alberta. The first phase's completion date is expected to be the fall of 1999.

In April 1998, the REIT provided $21.0 million in connection with the development of approximately 40 acres of land in Vaughan, Ontario for a retail centre anchored by a 130,000 square foot Wal-Mart store which was completed prior to the advance of funds.

Between April and December 1998, the REIT advanced $12.0 million to finance the development of a high-end retail outlet mall in Niagara Falls, Ontario. The first phase of this project, comprising approximately 75,000 square feet, is 100% occupied and open.

In August 1998, the REIT provided financing of $14.0 million in connection with the development of an office property in Dallas, Texas for office and telecommunications use.

Other mezzanine financings in 1998 included $6.0 million for the development of 47 acres in Mississauga, Ontario, an additional $5.0 million to begin construction on our original development project on Millcreek Drive, and $3.0 million for the development of a 68,678 square foot industrial property, also in Mississauga. The option to purchase this property was exercised after year–end.

Other Assets

Accounts receivable increased from $0.9 million at December 31, 1997 to $5.9 million at December 31, 1998 and deferred expenses increased from $2.0 million to $5.0 million over the same period. This increase parallels the growth in activity in the REIT, as well as, the accrual of interest on certain mortgage receivables.

Management's Discussion and Analysis

Prepaid expenses and sundry assets increased by $1.3 million from $1.5 million at December 31, 1997 to $2.8 million at December 31, 1998.

Certain leases call for rental payments that increase significantly over their term. Accrued rent receivable records the rental revenue from these leases on a rational basis, resulting in accruals for rent that are not billable or due until future years. Accrued rent receivable represents the adjustment for $2.1 million of rent from the Nestle lease at our 25 Sheppard Avenue West office building. This accrual has increased from $2.2 million at December 31, 1997 to $4.3 million at December 31, 1998, and will continue increasing until 2004 when the balance will begin decreasing until it reverts to zero at the lease's maturity in 2019. Each annual adjustment to this item affecting the income statement will be removed from the calculation of distributable income each year as it does not represent a cash item.

2121 Cornwall Road, Oakville

LIABILITIES

The REIT's Declaration of Trust limits the indebtedness of the Trust to a maximum of 60% of the Gross Book Value of the REIT (Gross Book Value is defined as the book value of the REIT's assets plus accumulated depreciation). At December 31, 1998, the REIT's indebtedness was 45% of the Gross Book Value of the REIT compared to 42% at December 31, 1997.

Mortgages payable increased to $284.3 million at December 31, 1998 compared to $188.9 million at December 31, 1997. The mortgages bear interest at the weighted average rate of 8.9% per annum (1997 - 10%) and mature between 1998 and 2018. To reduce risk, management has attempted to closely match the weighted average term to maturity of the mortgages of 10.6 years to the remaining average lease term of 9.4 years. Going forward, management anticipates the REIT will be able to renew its debt as it matures. Future principal payments are as follows:

1999	6.0%
2000	10.0%
2001	9.8%
2002	5.3%
2003	2.3%
Thereafter	66.6%

Year-end debt included bank indebtedness of $59.0 million, which bears interest at rates approximating bank prime. This debt is secured by fixed charges over certain income properties and is due on demand.

UNITHOLDERS' EQUITY

In 1998, two additional unit offerings were successfully completed. On May 21, 1998, the REIT finalized the sale of 8.5 million units for gross proceeds of $100 million. On December 10, 1998, a syndicate of underwriters exercised its over-allotment option to complete the sale of 4.6 million units for gross proceeds of $47.3 million.

These successful unit offerings allowed the REIT to add to its portfolio of assets, primarily through the use of equity rather than debt. As a result, the percentage of debt to Gross Book Value of assets was, as described above, substantially below the REIT's maximum level of indebtedness. This provides considerable debt capacity to fund future acquisitions.

LIQUIDITY & CAPITAL RESOURCES

During 1998, the REIT used a combination of new equity, conventional real estate debt, short-term financing and stable cash flow from its income producing properties to meet all of its liquidity requirements. Management expects to be able to meet all of the REIT's ongoing obligations and finance future growth in a similar fashion.

RISKS AND UNCERTAINTIES

The REIT has been structured to ensure that mandated investment guidelines and operating criteria are strictly adhered to. These policies govern such matters as the type and location of properties that the REIT can acquire, the maximum leverage allowed and the requirements for insurance coverage as well as environmental policies.

401-405 West Mall, Etobicoke

The REIT has maintained its ability to properly manage both operational and financial risks. The REIT's properties are leased under long-term arrangements to a diversified base of creditworthy tenants with strong covenants and are financed with long-term fixed rate mortgages.

No single tenant is critical to the REIT's ability to meet its financial obligations. The REIT's large, diverse tenant base allows it to fulfill its primary goal of maintaining a predictable cash flow.

Risk is further minimized through the maintenance of a low vacancy rate, relatively few short to medium-term lease renewals and a total debt restriction of 60% of aggregate assets. Furthermore, the REIT has adopted a conservative approach to financing its portfolio with the weighted average term to maturity of long-term debt closely matching the remaining average lease terms.

Since early 1998, we have been taking steps to ensure that all the computer management systems of the REIT and its property manager will continue to make date-related computations accurately on January 01, 2000 ("Y2K") and beyond. We completed our initial assessments in mid-1998. We have since completed an internal review of our management information systems (which operate our accounting and finance functions) and understand that our property manager has also completed its internal review of its critical systems. Based on those reviews, we believe such systems to be Y2K compliant. We are in the process of completing a detailed examination of our buildings and properties to determine the impact of Y2K on their computerized operational systems and what, if any, remediation plans are necessary or migration options available to achieve compliance. An assessment of the readiness of third parties such as significant tenants is also ongoing. As our significant tenants are primarily public entities, such assessment will include the review of their public disclosure records relating to the Y2K issue. We anticipate final completion of our Y2K plan, including the establishment of any necessary contingency plans, by June 1999 and are currently on target.

Although it is not possible to be certain that all aspects of the Y2K issue affecting the REIT, particularly those related to third parties, will be fully resolved, based on our examination to date, we do not anticipate any Y2K problems to have a material impact on our operations nor do we anticipate the costs to the REIT associated with the Y2K issue to represent a material amount. All such costs, which have so far been negligible in nature, will be appropriately expensed or capitalized as they are incurred, depending on the type of costs.

Management's Responsibility for Financial Reporting

The accompanying consolidated financial statements and information included in this Annual Report have been prepared by the management of H&R Real Estate Investment Trust which is responsible for their consistency, integrity and objectivity. The Trust maintains appropriate systems of internal control, policies and procedures to ensure that its reporting practices and accounting and administrative procedures are consistent, efficient and of a high quality.

KPMG LLP, the independent auditor, is responsible for auditing the consolidated financial statements and giving an opinion thereon.

The consolidated financial statements have been reviewed and approved by the Board of Trustees and the Audit Committee. This Committee meets regularly with management and the auditors who have full and free access to the Committee.

Thomas J. Hofstedter
President and Chief Executive Officer

Eric Cohen
Chief Financial Officer

Auditors' Report

TO THE UNITHOLDERS OF H&R REAL ESTATE INVESTMENT TRUST

We have audited the balance sheets of H&R Real Estate Investment Trust as at December 31, 1998 and 1997 and the statements of earnings, unitholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Trust as at December 31, 1998 and 1997 and the results of its operations and its cash flows for the years then ended in accordance with generally accepted accounting principles.

KPMG LLP

Chartered Accountants
Toronto, Canada
February 22, 1999

Balance Sheets

December 31, 1998 and 1997	1998	1997
		(In thousands of dollars)
ASSETS		
Income properties (note 2)	$ 585,297	$ 440,540
Mortgages receivable (note 3)	153,109	8,300
Other assets (note 4)	18,437	6,633
	$ 756,843	$ 455,473
LIABILITIES AND UNITHOLDERS' EQUITY		
Liabilities		
Mortgages payable (note 7)	$ 284,255	$ 188,909
Bank indebtedness (note 8)	59,004	1,225
Accounts payable	16,361	10,554
	359,620	200,688
Unitholders' equity		
38,968,649 units (1997 - 25,858,009) (note 9)	397,223	254,785
Contingency (note 16)		
	$ 756,843	$ 455,473

See accompanying notes to financial statements.

Approved by the Trustees

E Gilbert

Edward Gilbert
Trustee

Ronald C. Rutman
Trustee

Statements of Earnings and Unitholders' Equity

STATEMENTS OF EARNINGS

(In thousands of dollars, except per unit amounts)

Years ended December 31, 1998 and 1997	1998	1997
Operating revenue		
Rentals from income properties	$ 93,432	$ 62,012
Mortgage interest income and other	8,129	580
	101,561	62,592
Operating expenses		
Property operating costs	38,141	24,584
Mortgage interest	21,939	19,367
Depreciation of income properties	3,817	2,370
Amortization of deferred expenses	458	108
	64,355	46,429
Operating income from income properties	37,206	16,163
Trust expenses	3,147	1,744
	34,059	14,419
Instalment receipt interest income	-	2,041
Net earnings	$ 34,059	$16,460
Net earnings per unit (note 10)	$ 1.09	$ 0.84

See accompanying notes to financial statements.

STATEMENTS OF UNITHOLDERS' EQUITY

(In thousands of dollars)

Years ended December 31, 1998 and 1997	1998	1997
Unitholders' equity, beginning of year	$254,785	$143,807
Proceeds of offering of units	147,380	115,000
Issue costs	(6,759)	(6,722)
Discount on instalment receipts receivable	-	(402)
Net earnings	34,059	16,460
Distributions to unitholders	(32,242)	(13,358)
Unitholders' equity, end of year	$397,223	$254,785

See accompanying notes to financial statements.

Statements of Cash Flows

(In thousands of dollars)

Years ended December 31, 1998 and 1997	1998	1997
Cash provided by (used in)		
Operations		
Net earnings	$ 34,059	$ 16,460
Items not affecting cash		
Depreciation and amortization	4,275	2,478
Instalment receipt interest income	-	(2,041)
Gain on sale of income property	(365)	-
Cash flow from operations	37,969	16,897
Net changes in other operating items (note 11)	(5,980)	2,138
	31,989	19,035
Financing		
Bank loan	59,004	-
Mortgages payable		
Acquisitions	116,065	39,355
Repayments	(20,719)	(2,540)
Loan payable	-	(38,543)
Accounts payable	-	(4,391)
Proceeds of offering of units, net	140,621	107,876
Instalment receipts receivable	-	63,201
Distributions to unitholders	(32,242)	(13,358)
	262,729	151,600
Investments		
Income properties		
Proceeds on disposition	1,650	-
Acquisitions	(149,859)	(166,229)
Mortgages receivable	(144,809)	(8,300)
	(293,018)	(174,529)
Increase (decrease) in cash	1,700	(3,894)
Cash (bank indebtedness), beginning of year	(1,225)	2,669
Cash (bank indebtedness), end of year	$ 475	$ (1,225)

See accompanying notes to financial statements.

Notes to Financial Statements

(In thousands of dollars, except per unit and unit amounts)
Years ended December 31, 1998 and 1997

The Trust is an unincorporated trust with each unitholder participating pro rata in distributions of income and, in the event of termination of the Trust, participating pro rata in the net assets remaining after satisfaction of all liabilities.

1. Significant accounting policies

The financial statements have been prepared in accordance with generally accepted accounting principles in all material respects and reflect the following policies:

(a) Income properties
Income properties are recorded at the lower of cost less accumulated depreciation and net recoverable amount. Depreciation of buildings is recorded on the 5% sinking fund basis to fully amortize the cost of buildings over 40 years.

(b) Deferred expenses
Leasing costs, such as commissions, free rent and other tenant inducements, when incurred, are capitalized and amortized on a straight-line basis over the term of the related leases. Mortgage financing costs, when incurred, are deferred and amortized over the terms of the related debt.

(c) Co-ownerships
The Trust carries out a significant portion of its activities through co-ownership agreements and records its proportionate share of assets, liabilities, revenues, expenses and cash flows of all co-ownerships in which it participates.

(d) Income taxes
Pursuant to the terms of the Trust Agreement, the Trust intends to distribute its income for income tax purposes each year to such an extent that it will not be liable for income tax under Part I of the Income Tax Act (Canada). Therefore, no provision for income taxes is required.

(e) Use of estimates
The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. Actual results could differ from those estimates.

2. Income properties

	Cost	Accumulated depreciation	1998 Net book value	1997 Net book value
Land	$ 116,665	$ -	**$ 116,665**	$ 88,820
Buildings	474,845	6,213	**468,632**	351,720
	$ 591,510	$ 6,213	**$ 585,297**	$ 440,540

3. Mortgages receivable

The mortgages receivable are secured by real property under construction, bear interest at a weighted average of 9.9% (1997 - 10%) per annum and are repayable between 1999 and 2003. In most cases, the Trust has options to acquire an interest in the properties subject to mortgages.

4. Other assets

	1998	1997
Cash	$ 475	$ -
Accounts receivable	5,920	908
Prepaid expenses and sundry assets	2,791	1,544
Deferred expenses (note 5)	4,961	2,029
Accrued rent receivable (note 6)	4,290	2,152
	$ 18,437	$ 6,633

5. Deferred expenses

	Cost	Accumulated amortization	1998 Net book value	1997 Net book value
Leasing	$ 4,793	$ 544	$ 4,249	$ 2,029
Financing	727	15	712	-
	$ 5,520	$ 559	$ 4,961	$ 2,029

6. Accrued rent receivable

Certain leases call for rental payments that vary significantly over their term. The Trust records the rental revenues from these leases on a rational basis, resulting in accruals for rent that is not billable or due until future years. These amounts are recorded as accrued rent receivable.

7. Mortgages payable

The mortgages payable are secured by the income properties, bear interest at the weighted average rate of 8.85% (1997 - 10%) per annum and mature between 1998 and 2018. Future principal payments are as follows:

Year ending December 31	
1999	$ 17,114
2000	28,432
2001	27,892
2002	15,087
2003	6,704
Thereafter	189,026
	$ 284,255

Notes to Financial Statements

8. Bank indebtedness

	1998	1997
Bank loan	$ 59,004	$ -
Bank overdraft	-	1,225
	$ 59,004	$ 1,225

The bank indebtedness bears interest at bank prime, is secured by fixed charges over certain income properties and is due on demand.

9. Unitholders' equity

The beneficial interests in the Trust are represented by a single class of units which are unlimited in number. Each unit carries a single vote at any meeting of unitholders and carries the right to participate pro rata in any distributions.

H&R Developments and certain others, who are co-owners with the Trust in certain properties have the right and the obligation to exchange their interest in the properties, before 2017, for an aggregate of 5,870,000 units, subject to adjustment.

	Units issued and outstanding
As at December 31, 1996	15,700,000
Issued on June 10, 1997 (at a price of $10.00 per unit)	1,500,000
Issued on September 18, 1997 (at a price of $11.55 per unit)	8,658,009
As at December 31, 1997	25,858,009
Issued on May 21, 1998 (at a price of $11.75 per unit)	8,510,640
Issued on December 10,1998 (at a price of $10.30 per unit)	4,600,000
As at December 31, 1998	38,968,649

All units were issued for cash.

The following options were granted to independent trustees, officers and employees:

	Number of units 1998	Number of units 1997
$10.00, expiring in 2006	**895,000**	895,000
$10.84, expiring in 2007	**642,900**	642,900
$11.32, expiring in 2008	**570,532**	-
	2,108,432	1,537,900

As at December 31, 1998, no options were exercised.

10. Net earnings per unit

Net earnings per unit has been computed by dividing the net earnings by the weighted average number of units outstanding during the year of 31,305,938 units (1997 - 19,653,674).

11. Net changes in other operating item

	1998	1997
Accounts receivable	$ (5,012)	$ (832)
Accrued rent receivable	(2,138)	(2,152)
Deferred expenses	(3,390)	(2,137)
Prepaid expenses and sundry assets	(1,247)	(1,544)
Accounts payable	5,807	8,803
	$ (5,980)	$ 2,138

12. Risk management and fair value of financial assets and financial liabilities

(a) Risk management

The Trust is exposed to credit risk as an owner of real estate in that tenants may become unable to pay the contracted rents. Management mitigates this risk by carrying out appropriate credit checks and related due diligence on the significant tenants. Management has diversified the Trust's holdings so that it owns several categories of properties (office, industrial and retail) and is now acquiring properties outside of Ontario. In addition, management ensures that no tenant or related group of tenants accounts for a significant portion of the cash flow. The Trust is also exposed to credit risk as a lender on the security of real estate in the event that a borrower is unable to make the contracted payments. Such risk is mitigated through credit checks and related due diligence of the borrowers and through careful evaluation of the worth of the underlying assets.

(b) Fair values

The fair values of the Trust's accounts receivable and sundry assets, bank indebtedness and accounts payable approximate their carrying amounts due to the relatively short periods to maturity of the instruments.

The fair value of the mortgages receivable approximates carrying value since interest rates have not changed significantly since the mortgages were negotiated.

The fair value of the mortgages payable has been determined by discounting the cash flows of these financial obligations using December 31, 1998 market rates for debt of similar terms. Based on these assumptions, the fair value of mortgages payable at December 31, 1998 has been estimated at $292,402 compared with the carrying value of $284,255.

Notes to Financial Statements

13. Co-ownership activities

These financial statements include the Trust's proportionate share of assets, liabilities, revenues, expenses and cash flows as follows:

	1998	1997
Assets	$ 314,242	$ 287,947
Liabilities	176,371	161,274
Revenues	66,360	57,425
Expenses	47,003	39,820
Operating income from income properties	19,357	17,605
Cash flows generated by operating activities	21,291	20,236
Cash flows provided by financing activities	12,443	2,062
Cash flows used in investing activities	(24,552)	(9,472)

Under the terms of the co-ownership agreements, the Trust is only responsible for its proportionate share of the obligations of the co-ownerships.

14. Distributable income

Distributable income has been calculated in accordance with the terms of the Declaration of Trust as follows:

	1998	1997
Net earnings	$ 34,059	$ 16,460
Depreciation	3,817	2,370
Accrued rent	(2,138)	(2,109)
Imputed mortgage interest	202	220
Instalment receipt interest income	-	(2,041)
	$ 35,940	$ 14,900
Distributable income per unit	$ 1.15	$ 0.76
Cash distributions per unit	$ 1.03	$ 0.68

15. Related party transactions

The Trust has entered into agreements with H&R Property Management Ltd. (the "Property Manager"), a company affiliated with H&R Developments (note 9), to provide property management services concerning the properties owned by the Trust and support services in connection with the acquisition and development activities of the Trust. The initial term is five years and will be automatically renewed for three further terms of five years. During the year, the Trust paid fees pursuant to these agreements of $3,686 (1997 - $3,378), of which $932 (1997 - $1,329) were capitalized to the cost of the income properties acquired.

The Trust has a mortgage payable to Batise Investments Limited, a participant in H&R Developments, in the amount of $15,300 (1997 - $13,829). The related mortgage interest expense was $1,110 (1997 - $480).

During the year, the Trust entered into a mortgage receivable agreement with H&R Development Corporation, an affiliate of H&R Developments, to provide financing for the development of the TransCanada PipeLines Limited head office building. Pursuant to this agreement, the Trust advanced $65,000 (1997 - nil). The related interest income was $2,010 (1997 - nil).

16. Uncertainty due to the Year 2000 Issue

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure which could affect an entity's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the Trust, including those related to the efforts of customers, suppliers, or other third parties, will be fully resolved.

17. Comparative figures

Certain 1997 amounts have been reclassified to conform with the financial statement presentation adopted in 1998.

Trustees and Officers

Unitholder Information

H&R Real Estate Investment Trust

3625 Dufferin Street, Suite 500
Downsview, ON, Canada
M3K 1N4
Tel. (416) 635-7520
Fax (416) 398-0040

Registrar and Transfer Agent

CIBC Mellon Trust Company
P.O. Box 7010
Adelaide Street Postal Station
Toronto, ON M5C 2W9
Tel. (416) 643-5500 or 1-800-387-5501
Fax (416) 643-5501
E-mail: inquiries@cibcmellon.ca
Website: www.cibcmellon.ca

Auditors

KPMG LLP

Legal Counsel

Fraser Milner

Investor Information

Analysts, Unitholders and others seeking financial data should contact:
Eric Cohen,
Chief Financial Officer
at (416) 635-7520.

Taxability of Distributions

62 percent of the distributions made by the REIT to Unitholders during 1998 were tax deferred. Management estimates that 55 percent of the distributions to be made by the REIT in 1999 will be tax deferred.

Plan Eligibility

RRSP RRIF DPSP

Stock Exchange Listing

Units of H&R REIT are listed on The Toronto Stock Exchange under the trading symbol "HR.UN."

Annual Meeting of Unitholders

The Annual Meeting of Unitholders will be held at:
11:00 a.m. on May 27, 1999,
at The King Edward Hotel,
37 King Street East, Toronto, ON.

310-320-330 Front Street West, Toronto

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REIT